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# In the Supreme Court of the United States

OCTOBER TERM, 1945

No. **417**

DAIBY B. HORST, Executrix of the Estate  
of E. Clemens Horst, deceased,  
*Petitioner,*

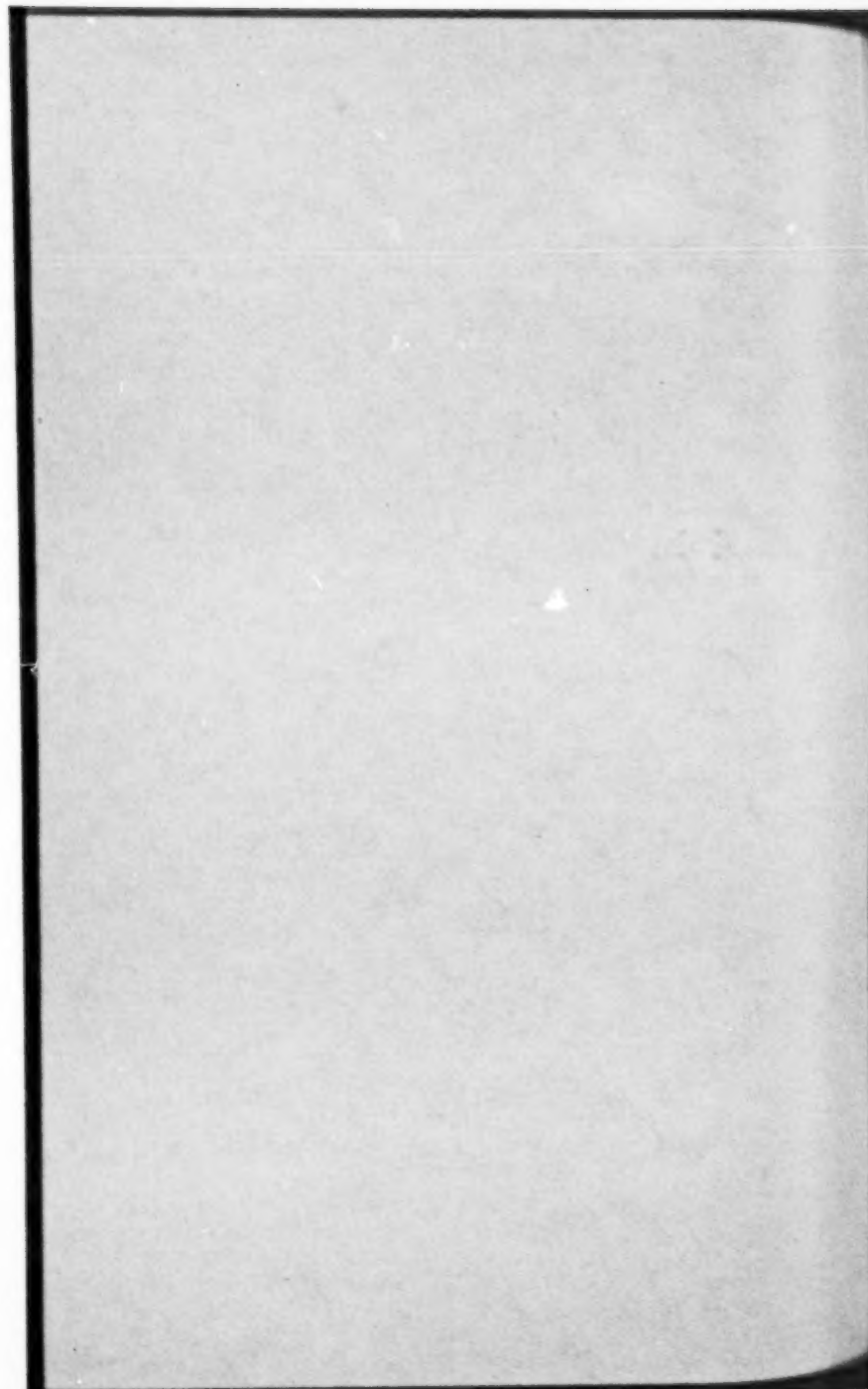
vs.

COMMISSIONER OF INTERNAL REVENUE,  
*Respondent.*

Petition for Writ of Certiorari to the United States  
Circuit Court of Appeals for the Ninth Circuit

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COMMISSIONER OF INTERNAL REVENUE,

*Respondent.*

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## **Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Ninth Circuit**

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*To the Honorable the Chief Justice and Associate Justices  
of the Supreme Court of the United States:*

The petition of Daisy B. Horst, Executrix of the Estate of E. Clemens Horst, deceased, respectfully shows:

This is a petition for a writ of certiorari to review a judgment of the United States Circuit Court of Appeals for the Ninth Circuit, which affirmed a decision of The Tax Court of the United States finding a deficiency of gift tax in the amount of \$9708 due from the petitioner.

**SUMMARY STATEMENT OF THE MATTER INVOLVED**

The Circuit Court of Appeals applied the wrong statute in deciding the case, with the result that its decision is at variance with the pronouncements of this Court, and also with decisions of the Circuit Court of Appeals for the Third Circuit.

The case involves the question whether the surrender by a wife to her husband of her interest in certain California community property acquired prior to 1927, was a "fair consideration in money or money's worth," within the meaning of Section 320 of the Revenue Act of 1924, for his conveyance of other similar community property to her as her separate property.

The Circuit Court of Appeals based its decision entirely upon the gift tax provisions of the Revenue Act of 1932, which differed in language and meaning from the gift tax provisions of the statute applicable here, the Revenue Act of 1924. The Revenue Act of 1924 required only a "fair consideration" to exempt a transfer from tax; the Revenue Act of 1932 required an "adequate and full consideration." The court held that the surrender of the wife's interest was not an "adequate and full consideration," and that therefore a tax was due on the transfer by the husband.

**OPINIONS BELOW**

The decision of The Tax Court (R. 25), is reported in 3 Tax Court of the United States Reports, page 417. The decision of the United States Circuit Court of Appeals for the Ninth Circuit (R. 43) had not been reported at the time this petition was prepared.

### JURISDICTION

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 (28 U.S.C. 347), and under Section 1141(a) of the Internal Revenue Code (26 U.S.C. 1141(a)).

The judgment of the United States Circuit Court of Appeals was entered June 5, 1945 (R. 47). A timely petition for rehearing was filed, and was denied August 2, 1945 (R. 48). On August 7, 1945, the Court entered an order staying its mandate to The Tax Court until after this Court passes upon a petition for certiorari, if such petition be filed on or before September 15, 1945.

### STATUTES INVOLVED

The transfer involved here was made in 1925; the applicable statute was therefore the Revenue Act of 1924 (43 Stat. 313 et seq.). Section 319 of that Act imposed a tax upon transfers "by gift \* \* \* of any property" (43 Stat. 313). Section 320 of the Act provided in part:

"Where property is sold or exchanged for less than *a fair consideration in money or money's worth* then the amount by which the fair market value of the property exceeded the consideration received, shall \* \* \* be deemed a gift." (43 Stat. 314).

The Revenue Act of 1924 became effective on June 2, 1924 (43 Stat. 253) and its gift tax provisions were in effect until January 1, 1926. They were repealed effective as of the latter date by Section 1200 of the Revenue Act of 1926 (44 Stat. 125).

The Revenue Act of 1932 became effective on June 6, 1932; and its gift tax provisions applied only to transfers

made after that date (Revenue Act of 1932, Sec. 501(a) and (b), 47 Stat. 245).

Section 503 of the Revenue Act of 1932 provided in part:

“Where property is transferred for less than an *adequate* and *full* consideration in money or money’s worth, then the amount by which the value of the property exceeded the value of the consideration, shall \* \* \* be deemed a gift \* \* \*.” (47 Stat. 247).

Section 503 of the Revenue Act of 1932, requiring an “adequate and full” consideration to exempt a transfer from tax, was the statute relied upon by the Ninth Circuit Court of Appeals, instead of the statute that obviously applied, §320 of the Revenue Act of 1924, which required only a “fair” consideration.

#### QUESTIONS PRESENTED

The questions are:

1. Whether the court below erred in upholding a gift tax assessment on the ground that the transfer in question was not supported by an “adequate and full consideration,” where the applicable statute purported to tax only such transfers as were not supported by a “fair consideration.”

2. Whether the surrender by a wife to her husband of her community interest in certain California community property acquired prior to 1927 was a “fair consideration in money or money’s worth” (within the meaning of Section 320 of the Revenue Act of 1924), for his transfer of similar community property to her as her separate property.



**REASONS FOR GRANTING THE WRIT**

The effect here given to Section 320 of the Revenue Act of 1924 is, we submit, in conflict with the decisions of this Court and also with decisions of another Circuit Court of Appeals on the same matter.

The decision imposes a tax on a transfer which the statute did not intend, since the consideration given was a "fair consideration in money or money's worth," under the authorities, and that is all the statute required.

By deciding the case on the basis of the wrong statute, the court in effect failed to afford petitioner the review of The Tax Court's decision to which petitioner is entitled. The court below thus so departed from the usual course as to call, we submit, for exercise of this Court's supervisory powers.

**STATEMENT OF THE CASE**

In 1925 E. Clemens Horst and Daisy B. Horst, who were married in 1893, and were residents of California (R. 23), owned 4052 shares of the stock of E. Clemens Horst Company. On April 11, 1925, by an agreement in writing, E. Clemens Horst conveyed 2026 shares of this stock to Daisy B. Horst as her separate property, in consideration of her conveyance of the remaining 2026 shares to him as his separate property (R. 23).

Respondent determined that the transaction constituted a taxable gift of 2026 shares by E. Clemens Horst, and accordingly asserted a deficiency of gift tax under the Revenue Act of 1924. Petitioner filed a timely petition to The Tax Court, which upheld the Commissioner's determination (R. 21, 27).

### The Tax Court's Decision

The Tax Court did not construe the term "fair consideration in money or money's worth," contained in Section 320 of the Revenue Act of 1924, although this was a vital issue in the case. Nor did The Tax Court make an independent analysis of the nature or incidents of a wife's interest in California community property acquired prior to 1927, so as to determine whether her interest is sufficiently substantial and valuable prior to the husband's death to meet the statutory requirement of a "fair" consideration.

Instead, The Tax Court relied upon a decision of the Ninth Circuit Court of Appeals, *Gillis v. Welch* (C.C.A. 9th, 1935) 80 F.(2d) 165, Cert. Den. 297 U.S. 722, which The Tax Court thought compelled the conclusion that a wife had "no estate of value" (R. 26) in California community property acquired prior to 1927,\* and that therefore Mrs. Horst's surrender of her community rights in the shares (which thereby became Mr. Horst's separate property), did not constitute any consideration for the transfer by him to her of other shares (R. 25).

In fact, what the *Gillis* case held was that the wife had no vested property interest in such community property, and that therefore a gift of such property by a husband to his wife constitutes a gift of the whole property. The court had no occasion to consider the vital question

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\*California Civil Code, Section 161a, which gave the wife a vested interest in community property (*U. S. v. Malcolm* (1931), 282 U.S. 792), did not become effective until July 28, 1927, and did not apply to the community property acquired prior to that date. *Spanfelner v. Meyer* (1942), 51 Cal. App.(2d) 390. The community stock involved in this case was, of course, acquired prior to 1927; and hence Mrs. Horst's interest in it was not vested.

in the present case, namely, whether the wife's legal rights with respect to such community property are sufficiently substantial for their release by her to constitute a fair consideration.

Otherwise stated, the question in the *Gillis* case was, what passes on a transfer of community property by a husband to his wife;—the question here is whether the rights surrendered by a wife, when she surrenders her rights with respect to such community property, are sufficiently substantial to constitute a fair consideration.

It follows\* that neither the premise nor the conclusion in the *Gillis* case is relevant here. *A fortiori*, The Tax Court erred in holding that the *Gillis* case compelled the result reached.

#### Decision of the Court Below

The Circuit Court of Appeals affirmed the decision of The Tax Court, but on a wholly different ground, namely, that the test to be applied is whether there was a “adequate and full consideration” for the conveyance by Mr. Horst. As shown above, this is the requirement imposed by the gift tax provisions of the Revenue Act of 1932, as contrasted with “fair consideration,” all that was acquired by the Revenue Act of 1924, the applicable statute.

The opinion of the court below is not wholly clear, but does plainly rest the decision on the 1932 Act. The court relies for its conclusion on the decisions of this Court in *Commissioner v. Wemyss* (1945), 324 U.S. 303, and *Merrill v. Fahs* (1945), 324 U.S. 308, both decided under the 1932 Act. Speaking first of *Merrill v. Fahs*, the court below says,

"The Supreme Court decided that the phrase 'an adequate and full consideration in money or money's worth' came into the gift tax by way of estate tax provisions. In interpreting the estate tax provision, the Supreme Court said Congress intended the phrase 'an adequate and fair consideration in money or money's worth' to exclude dower and other marital rights, citing *C. I. R. v. Bristol*, 121 F.(2d) 129, and *Sheets v. C. I. R.*, 95 F.(2d) 727. In the *Merrill* case, the Supreme Court held that the same words in the gift tax should be given the same meaning." (R. 46)

It will be observed that the court below first makes reference, in quotation marks, to the phrase, "adequate and full consideration" (which is the term used in the 1932 Act), and in the following sentence to "adequate and fair consideration." The latter phrase, so far as we are aware, does not appear in any statute or relevant case. In any event, the court below plainly held that consideration for such a transfer must be, among other things, "adequate" (which simply was not true under the statute applicable here); and rests its decision on cases in which this Court applied the 1932 Act requiring "adequate and full consideration."

Like The Tax Court (but doubtless for different reasons since it was applying the wrong statute), the court below expressed the view that the surrender by the wife of her community interest in California community property acquired prior to 1927 could not be consideration within the meaning of the Act, because the wife's interest was not a "vested" interest. The court said (R. 44):

"In California, until the adoption of Section 161a of the Civil Code in 1927, the wife had no vested

interest. [Citing cases] It follows therefore that E. Clemens Horst owned the entire holding of stock and by this instrument merely gave one-half of his stock to his wife."

But as shown above, the conclusion does not follow, the question here being whether the rights, powers and privileges which the wife surrendered (whether denominated "vested" property rights or not), constituted fair consideration for the transfer which she received in exchange.

**The controlling questions were  
not passed on by either court  
below.**

The controlling questions are: (a) the scope of the term "fair consideration" in the Revenue Act of 1924, and (b) the question whether the wife's surrender of her rights and powers with respect to California community property acquired prior to 1927 is of sufficient value to constitute "fair" consideration for the transfer to her by her husband of similar community property.

The foregoing summary of the decisions below is sufficient, we believe, to show that neither of these questions was really passed upon by either court. We will not stop further to analyze the opinions below on this question, since both are very short (R. 25), (R. 43).

**Under California law, the wife's  
community property interest  
was of substantial value.**

It is unnecessary to labor the point that although the question, whether the surrender of the wife's community property rights was a "fair consideration," is a federal

question, the qualities of the wife's rights thus surrendered is determined by the law of the State of California.

The substantial value of the wife's rights, powers and privileges with respect to such community property, is sufficiently shown by the case of *Estate of Brix* (1919), 181 Cal. 667, dealing with community property acquired prior to 1927.

That case, moreover, is persuasive authority directly on the question whether the surrender of the wife's interest supplies a "fair consideration,"—this because it held that under the state inheritance tax act, a transfer of community property by husband and wife was not a taxable transfer "without valuable and adequate consideration" where made in consideration of the wife's surrender of her community rights.

The court's summary of the group of rights which the wife transferred when she surrendered her rights with respect to such community property, reads as follows:

"While the wife has no title to the community property nor estate or interest therein, yet she has rights in relation thereto, the surrender of which may constitute a valuable and, according to the circumstances of the case, an adequate consideration for the transfer. She has a 'possible interest in whatever remains upon the dissolution of the community otherwise than by her own death.' (In re Burdick, 112 Cal. 393 (44 Pac. 735).) Upon the death of the husband she takes one-half of the community property and upon a divorce she may, in a proper case, be awarded even the whole of it. (Civ. Code, secs. 146, 1402.) If a divorce is granted without any disposition of the community property, the former wife becomes the owner of one-half of the community property as tenant in

common with her former husband. [Citing cases] If the husband makes a gift of community property without the wife's consent she may upon his death recover from the donee one-half of the property so given. (Civ. Code, sec. 172; *Dargie v. Patterson*, supra.) The fact that she may thus attack a conveyance by the husband made without her consent, on the ground that it was a gift, has a practical application that renders it a great disadvantage to a husband not in cordial relations with his wife. It has become the universal custom with purchasers of real property to insist on her signature to all contracts relating thereto. The custom is so general that it is a matter of common knowledge of which the court may take judicial notice.\* [Citing cases] In the actual dealings of the husband in community real estate this gives her a practical control or power of interference which may be a great burden to him." (181 Cal., pp. 674, 676)

It is unreasonable (we submit) to say that the surrender by the wife of rights, powers and privileges, including all of those enumerated in the passage just quoted, does not constitute a "fair consideration."

The history of the revenue acts emphasizes that "fair" consideration need not be either "full" or "adequate."

Two decisions by this Court trace the history of a number of parallel provisions in the estate and gift tax laws, namely, *Taft v. Commissioner* (1938), 304 U.S. 351 and

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\*Since 1917 the statute has required that the wife join in any conveyance or encumbrance or community real property, or any lease of it for a period of more than one year. Cal. Civ. Code, Sec. 172a.

*Merrill v. Fahs* (1945), 324 U.S. 308. They show that various provisions dealing with the consideration for transfers of one kind or another, have appeared in the estate law since at least as early as 1916, and in the gift tax law since 1924; that the changes made in the two laws from time to time were closely related, and that substitution of the requirement of "adequate and full consideration," in place of the former provision requiring merely "fair" consideration, effected a substantial change in the law.

The Revenue Acts of 1916, 1918 and 1921 contained estate tax provisions allowing deductions for claims against the estate if "allowed by the laws of the jurisdiction \* \* \* under which the estate is being administered." The Acts of 1916, 1918, 1921 and 1924 excepted from taxable transfers in contemplation of death, sales for a "fair consideration in money or money's worth." The Act of 1924 changed the provision concerning deductible claims against the estate, so as to permit deduction only of claims supported by a "fair consideration in money or money's worth." The Act of 1924 used this same phrase with respect to the gift tax, first imposed by that act.

In 1926 (the courts having held that a release of inchoate dower rights was a "fair consideration"), the provision in the estate tax law concerning deductible claims, and also that concerning transfers in contemplation of death, were changed to require "adequate and full" consideration. This language was adopted when the gift tax was revived in 1932 (there having been no gift tax from 1926 to 1932).

In the *Taft* case, *supra*, the Court said:

"Congress had reason to think that the phrase 'fair consideration' would be held to comprehend an in-



stance of a promise which was honest, reasonable, and free from suspicion whether or not the consideration for it was, strictly speaking, adequate.\* The words 'adequate and full consideration' were substituted by §303(a)(1) of the Act of 1926. There must have been some reason for these successive changes. It seems evident that the purpose was to narrow the class of deductible claims, and we are not at liberty to ignore this purpose." (304 U.S., pp. 355, 356)

In *Merrill v. Fahs*, *supra*, the Court said, in part:

"The two types of tax thus followed a similar course, like problems and purposes being expressed in like language. In this situation, courts held that 'fair consideration' included relinquishment of dower rights. [Citing cases] Congress was thus led, as we have indicated, to substitute in the 1926 Revenue Act, the words 'adequate and full consideration' in order to narrow the scope of tax exemptions. [Citing cases]"

Since the *Merrill* case is so recent, we refrain from further analysis of the opinion therein; but call attention to the fact that the whole opinion bears directly on the questions here presented, the decision in this case being, as we submit, in conflict therewith.

**This decision conflicts with  
decision of another Circuit  
Court of Appeals.**

The decision below is, we submit, in conflict with the decisions of the Circuit Court of Appeals for the Third Circuit in *Ferguson v. Dickson* (C.C.A. 3d, 1924), 300 F.

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\*Citing *Ferguson v. Dickson*, *infra*.

961, cert. den. 266 U.S. 628, and *McCaughn v. Carver* (C.C.A. 2d, 1927), 19 F.(2d) 126.

Both *Ferguson v. Dickson* and *McCaughn v. Carver*, *supra*, held that the relinquishment of inchoate marital rights in property (in these cases inchoate dower) was a fair consideration in money or money's worth within the meaning of the estate tax provisions of the Revenue Act of 1918. *Ferguson v. Dickson* defined a fair consideration as "a consideration which under all the circumstances is honest, reasonable, and free from suspicion, whether or not strictly 'adequate or full.'" 300 F. 964. This definition was confirmed by *McCaughn v. Carver*, in which the Court said:

"The substantial element the law considers is not so much the form as the good faith and the fair construction of the transaction." (19 F.(2d) 127)

These cases cannot be reconciled with the decision in the instant case. Inchoate dower, and the wife's rights in California community property acquired prior to 1927, are very similar in nature during the husband's lifetime. Neither of them becomes vested until the husband's death; neither of them ripens into possession or enjoyment until that time, but they both have certain incidents during the husband's lifetime that make them substantial and valuable. Indeed, a careful analysis of the two interests shows that the wife's interest in community property is the more valuable and substantial of the two.

And independently of those cases, it is, we believe, apparent that, under California law, the wife's rights and powers with respect to such property are substantial indeed; and their surrender constitutes fair consideration

for the husband's transfer of other property, as was held by the Supreme Court of California in a similar case.

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### CONCLUSION

It is submitted that the writ should be granted because of the conflict between the decision in this case, on the one hand, and the decisions of this Court and the Circuit Court of Appeals for the Third Circuit, on the other; and in order that a proper review of the decision of The Tax Court may be had on the basis of consideration of the controlling statute, which was in effect ignored by the court below.

Dated: San Francisco, California,  
September 8, 1945.

Respectfully submitted,

MAURICE E. HARRISON,  
*Attorney for Petitioner.*

THEODORE R. MEYER,  
ROBERT H. WALKER,  
*Of Counsel.*

*Due service and receipt of a copy of the within is hereby  
admitted this \_\_\_\_\_ day of September, 1945.*

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*Attorney for Respondent*